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Cotton and Products

Annual Report

2004

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Report Highlights:
Mexican cotton production is expected to increase by approximately 75 percent to 625,000 bales in MY 2004/05 (Aug-Jul), due to higher world cotton prices and expected increases in government supports. Imports are forecast to increase slightly to 2.150 million bales, as a result of the recovery in the U.S. economy and the consequent increase in Mexico's textile/apparel exports.

Includes PSD Changes: Yes
Includes Trade Matrix: Yes
Annual Report
Mexico [MX1]
[MX]

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SECTION I. SITUATION AND OUTLOOK

Mexican cotton production for MY 2004/05 is forecast at 625,000 bales (480 lb./bale), an increase of 75 percent from the revised estimate of MY 2003/04, due to higher world cotton prices, increased planted area, and expectations of increased government supports. According to the Confederation of Mexican Cotton Associations (CMCA*),* its planting intentions survey revealed that Mexican producers have increased cotton acreage by approximately 84 percent. It should be noted, however, that this production forecast accounts for just 32 percent of total consumption, with the rest coming from imports. Moreover, this production forecast remains substantially below the average production levels of the late 1990s. Production levels and planted area for the previous two years were atypically low due to unattractive international prices. The production estimates and harvested area for MY 2002/03 and 2003/04 were revised upward reflecting new official information from the Secretariat of Agriculture, Livestock, Rural Development, Fisheries and Foodstuffs (SAGARPA) as well as from private sources.

Domestic demand for cotton is forecast at 2.150 million bales in MY 2004/05, up approximately 2.3 percent from MY 2004/05. Consumer demands for textile products will likely increase next year as result of the recovery of the U.S. economy and a weaker peso. According to private industry sources, Mexico's cotton industry is sensitive to the effects of the depreciating Mexican peso, which increased the competitive advantage of Mexico's textile exports to the United States. The peso has devalued by about 10 percent against the dollar since last year. A main user of Mexican cotton is the textile industry. The estimate for total cotton consumption in MY 2002/03 and 2003/04 remained unchanged.

Compared to MY 2003/04 (Jul-Aug), Mexico is expected to import approximately one percent more cotton and exports are expected to remain constant in MY 2004/05. Two main factors limiting demand for cotton imports are: 1) growing low-cost competition from China affecting Mexico's apparel/textile exports to the United States; and 2) illegal apparel/textile imports, mainly from Asian countries. Despite the fact that the Mexican government has increased its efforts to deter illegal imports, private sources pointed out that major measures have yet to be implemented. The cotton import and export estimates for MY 2002/03 have been revised upward according to official information form the Secretariat of Economy (SE). Similarly, the MY 2003/04 cotton import estimate has been revised slightly downward, reflecting more recent information from industry sources. These industry sources stated that, as of April 2004, Mexican MY 2003/04 imports totaled approximately 972,000 bales, leaving an estimated 719,300 bales of imports still anticipated before the end of July 2004. With less than five months remaining in the marketing year, weekly shipments need to average 51,300 bales in order to reach this import target, which is highly unlikely, according to these industry sources. As usual, practically all of the imports will be sourced from the United States. Mexican exports of cotton to traditional markets in Asia are expected to remain unchanged from the revised estimate of MY 2003/04, at 100,000 bales. With a slight increase in mill use in MY 2004/05, ending stocks are projected to decline to 563,000 bales, tightening the stocks-to-use ratio to 25.9 percent, compared to a 32.8-percent stocks-to-use ratio in MY 2003/04.

In reference to the economy, for the fourth quarter of 2003 and the beginning of 2004 Mexico's economy grew slightly more-than-expected in quarterly annualized terms. Private analysts indicate that the 1.3-percent GDP growth registered in 2003 was low and kept per-capita income stagnant. However, the result from the last quarter of 2003 is encouraging and economists forecast 2004 growth at 3.2 percent. At the same time, inflation has been reduced over the last few years due to tighter controls of the money supply. These factors should bolster textile fiber consumption. Analysts pointed out that reviving Mexico's textile/apparel exports would depend on continued U.S. economic growth, as well as on Mexico's ability to compete with China.

SECTION II. STATISTICAL TABLES

PSD Table						
Country	México					
Commodity	Cotton				(HECTARES)(MT)	
	2002 Revised		2003 Estimate		2004 Forecast	
	USDA Official [Old]	Post Estimate [New]	USDA Official [Old]	Post Estimate [New]	USDA Official [Old]	Post Estimate [New]
Market Year Begin	08/2002		08/2003		08/2004	
Area Planted	0	42351	0	63763	0	117300
Area Harvested	38000	41494	58000	62430	0	103100
Beginning Stocks	157199	157199	226653	231484	147183	151767
Production	42239	44666	67495	77722	0	136000
Imports	500771	507946	342919	327000	0	330000
TOTAL SUPPLY	700209	**709811**	637067	**636206**	147183	**617767**
Exports	10886	15658	27216	21770	0	21770
USE Dom. Consumption	457226	457226	457226	457226	0	468055
Loss Dom. Consumption	5443	5443	5443	5443	0	5443
TOTAL Dom. Consumption	462669	462669	462669	462669	0	473498
Ending Stocks	226653	231484	147183	151767	0	122499
TOTAL DISTRIBUTION	700208	**709811**	637068	**636206**	0	**617767**

PSD Table						
Country	Mexico					
Commodity	Cotton		HECTARES & 480 lb Bal		Conversion 0.00459291	
	Revised 2001		Estimate 2002		Forecast 2003	
	USDA Official [Old]	Post Estimate [New]	USDA Official [Old]	Post Estimate [New]	USDA Official [Old]	Post Estimate [New]
Market Year Begin	08/2002		08/2003		08/2004	
Area Planted	0	42351	0	63763	0	117300
Area Harvested	38000	41494	58000	62430	0	103000
Beginning Stocks	722090	722090	1041125	1063316	676082	697138
Production	194024	205172	310037	357014	0	624713
Imports	2300280	2333238	1575191	1502067	0	1515847
TOTAL SUPPLY	3126394	**3260501**	2926353	**2922398**	676082	**2837699**
Exports	50005	71925	125016	100000	0	100000
USE Dom. Consumption	2100257	2100257	2100257	2100257	0	2150000
Loss Dom. Consumption	25002	25002	25002	25002	0	25002
TOTAL Dom. Consumption	2125260	2125260	2125260	2125260	0	2175002
Ending Stocks	1041125	1063316	676082	697138	0	562696
TOTAL DISTRIBUTION	3216390	**3260501**	2926357	**2922398**	0	**2837699**

Cotton	H.T.S. 5201		UNITS: MT
EXPORTS	MY 2001/2002	MY 2002/2003	MY 2003/2004①
TO:			
U.S.	**3,360**	**537**	**1,741**
OTHER			
JAPAN	8,044	7,276	4,180
GUATEMALA	5,203	1,856	672
TOTAL OF OTHER	13,247	9,132	4,852
OTHERS NOT LISTED	2,709	5,989	5,367
GRAND TOTAL	19,316	15,658	11,960

SOURCE: World Trade Atlas, Mexico Edition, January 2004.
MY begin August ends July. ①Data as of January 2004

Cotton	H.T.S. 5201		UNITS: MT
IMPORTS	MY 2001/2002	MY 2002/2003	MY 2003/2004①
FROM:			
U.S.	**442,777**	**503,594**	**150,111**
OTHER			
CAMEROON	5,723	2,602	0
MALI	1,064	1,748	527
TOTAL OF OTHER	6,787	4,350	527
OTHERS NOT LISTED	101	2	1
GRAND TOTAL	449,665	507,946	150,639

SOURCE: World Trade Atlas, Mexico Edition, January 2004.
MY begin August ends July. ①Data as of January 2004

Cotton Yarn	H.T.S. 5205, 5206, 5207		UNITS: Kg
Exports to:	CY 2002	CY 2003	CY 2004①
UNITED STATES	**20,017,944**	**24,974.813**	**2,047.168**
OTHER			
CANADA	864,865	533.399	54.803
DOMINICAN REPUBLIC	91	50.963	0
FRANCE	24,784	3	0
TOTAL OTHER	889,740	584.365	54.803
OTHER NOT LISTED	77,370	378.281	41.464
GRAND TOTAL	**20,985,054**	**25,937.459**	**2,143.435**

SOURCE: World Trade Atlas, Mexico Edition, February 2004.
①Data as of January 2004.

Cotton Yarn	H.T.S 5205, 5206, 5207		UNITS: Kg
Imports from:	CY 2002	CY 2003	CY 2004①
United States	**23,513,149**	**13,391.873**	**964.078**
OTHER			
TAIWAN	1,166,603	1,236.322	29.902
SPAIN	1,076,235	970.874	157.474
TOTAL OTHER	2,242,838	2,207.196	187.376
OTHER NOT LISTED	1,919,865	3,166.628	457.702
GRAND TOTAL	**27,675,852**	**18,765.697**	**1,609.156**

SOURCE: World Trade Atlas, Mexico Edition, February 2004.
①Data as of January 2004.

Woven Cotton Fabrics Kg & M^2	H.T.S. 5208, 5209, 5210, 5211, 5212		UNITS:
Exports to:	CY 2002	CY 2003	CY 2004①
United States	**93,908,124**	**46,217.080**	**2,707.363**
OTHER			
CANADA	4,518,907	2,703.852	111.542
EL SALVADOR	1,386,932	454.279	35.964
COLOMBIA	2,257,603	1,458.739	108.116
GUATEMALA	1,423,976	210.282	24.939
TOTAL OTHER	9,587,418	4.827.152	280.561
OTHER NOT LISTED	23,499,253	2,899.736	202.938
GRAND TOTAL	**126,994,795**	**53,943.968**	**3,190.862**

SOURCE: World Trade Atlas, Mexico Edition, February 2004.
①Data as of January 2004.
Note: To comply with WTO directives regarding the harmonized tariff system' homologation, official data for CY 2003 & CY 2004 is shown in M^2. Starting CY 2003 all Woven Cotton Fabrics' amounts are reported in M^2. For CY 2002 figures are in Kg.

Woven Cotton Fabrics H.T.S. 5208, 5209, 5210, 5211, 5212 UNITS: M^2			
Imports from:	CY 2002	CY 2003	CY 2004①
United States	**490,479,631**	**434,065.954**	**26,572.264**
OTHER			
SOUTH KOREA	24,027,620	38,820.571	986.907
CHINA	59,369,719	66,880.913	4,456.960
INDIA	35,119,009	17,891.328	2,051.817
TOTAL OTHER	118,516,348	123,592.812	11,495.684
OTHER NOT LISTED	118,006,490	118,305.528	8,797.685
GRAND TOTAL	**727,002,469**	**675,964.294**	**46,865.633**

SOURCE: World Trade Atlas, Mexico Edition, February 2004.
①Data as of January 2004.

SECTION III. NARRATIVE ON SUPPLY, DEMAND, POLICY, & MARKETING

PRODUCTION

MY 2004/05 cotton production is forecast at 625,000 bales (480 lb/bale), a 75-percent increase from MY 2003/04 production, due to higher international prices, increased planted area, and expectations of increases in government supports. As a result, producers believe that approximately 177,000 hectares will be planted in MY 2004/05, an 84-percent increase above the revised MY 2003/04 planted area figure of 63,763 ha. It should be noted that production and planted area for the previous two years were atypically low due to unattractive international prices. According to the CMCA, the target price could be increased to approximately U.S. $0.68 per pound of cotton lint during the MY 2004/05. In MY 2003/04, the target price for cotton was U.S. $0.64 per pound of cotton lint (see MX2173, MX3098 and MX3131). It should be noted that growers insist that they would not be able to produce cotton without this type of government support.

The increase in planted area is particularly true for producers in the Juarez and Delicias areas, in the state of Chihuahua, where the forecast for planted area has increased from 29,100 hectares in MY 2003/04 to approximately 45,000 hectares for MY 2004/05. As a result, cotton production in this area could reach nearly 241,000 bales. Also, production in the Mexicali/San Luis area is expected to increase to 100,000 bales, up from 80,663 bales last year, due to increased acreage. The CMCA pointed out that farmers in the La Laguna region (comprised of the states of Coahuila and Durango) are going to plant approximately 18,000 hectares of transgenic cotton in April and May of 2004. Preliminary planting figures in the south of Sonora estimate that approximately 14,000 hectares will be planted, despite a water shortage for crop irrigation. According to CMCA, cotton areas will be irrigated by wells in southern Sonora. Also, the Sinaloa state government project to improve the hydraulic infrastructure in the Yaqui and Mayo valleys has also contributed to the increase in cotton planted area. However, other areas, namely, in the north and south of the state of Tamaulipas, cotton production is expected to be lower than initially forecast, due to dry weather conditions.

According to official sources, approximately 25,000 hectares were planted with BT cottonseed during the MY 2003/04, which helped offset some production costs. Alcala and Delta Pine are the most popular seed type used by cotton growers and only a small proportion of Pima variety is planted in Juarez region. All seeds are imported from the United States. According to CMCA, in the last few years' growers have used fast-maturing seed varieties to compensate for dry weather conditions in some areas such as in Sinaloa.

Production and harvested area estimates for MY 2002/03 and 2003/04 have been revised upward in line with updated official information from Mexico's Secretariat of Agriculture, Livestock, Rural Development, Fisheries and Foodstuffs (SAGARPA) and the CMCA.

PRODUCTION POLICY

During MY 2003/04, cotton producers received government subsidies under the terms of PROCAMPO (the governmental income support program for farmers) as well as direct support through the "Target Income" program (i.e., target price) (see Production section). For MY 2004/05 these subsidies will continue. On March 1, 2004, SAGARPA announced it will pay producers of cotton and other crops 935 pesos (USD $85) per hectare during the 2004/04 spring/summer and the 2004/05-fall/winter planting seasons under the PROCAMPO domestic support program. This payment is 3.3 percent greater than what SAGARPA paid during the same period in 2003/04. The announcement also indicates that farmers with producing areas of between one and five hectares will receive 1,120 pesos (USD $102) per hectare, or 8.7 percent more than SAGARPA paid last year.

Also, on July 14, 2003, SAGARPA announced specific guidelines establishing the mechanisms to provide supports to producers of cotton and other products (see MX3098 and MX3131). These supports are part of the "Target Income" Program (see MX2173 and MX3067). These guidelines are based on the general Operational Regulations (REGLAS) that SAGARPA published for several support programs on June 17, 2003. According to these Operational Regulations, the objective of the "Target Income" program is to provide price certainty to farmers, increase their market competitiveness and, consequently, their economic profitability. Other objectives are to encourage farmer diversification and integration into agricultural food chains, and regional development.

YIELDS AND INPUTS

The yields around the country traditionally vary. The overall average yield for the MY 2003/04 cotton crop, however, was 5.7 bales/ha, with yields varying between 3.7 and 6.8 bales per hectare. Cotton yields for MY 2004/05 are expected to reach 6.1 bales/ha, assuming normal weather conditions and good water availability. Cotton production takes place mostly in northwest Mexico, where crop irrigation is required.

Similarly, costs of production for cotton vary according to areas. In Ciudad Obregon, Sonora, for example, costs are estimated at approximately 14,000 pesos/ha (roughly US$ 1,231/ha). While in the La Laguna area costs are reportedly 19,000 pesos/ha. (US$ 1,671) According to the CMCA, average costs are estimated at 9,000 pesos/ha (US$ 792 /ha). The CMCA also pointed out that, in general, production costs are higher than those in the United States, despite the fact that an increase in the use of BT cottonseed in some Mexican cotton-growing areas has helped offset some production costs. According to industry sources, Mexican cotton quality is generally poor and inconsistent. Although there are approximately 150 gins, the majority of these are outdated and damage the cotton during the ginning process. Textile firms use the High Volume Instrument testing (HVI), but not the growers. Consequently, only smaller mills use Mexican cotton, with products designed toward the domestic market. While large mills generally consume U.S. cotton in its production process, as U.S. cotton is considered to be more consistent and of better quality.

CONSUMPTION

For MY 2004/05, consumption is expected to increase slightly to 2.150 million bales over the current year. The increase in consumption is attributed to the recovery in the Mexican economy and an increase (albeit to a lesser extent) of textile exports to the U.S. The United States continues to be the principal market for Mexico's textile exports, accounting for 98.5 percent of total exports. Some industry sources expect a slight increase in their exports to the United States, mainly of denim jeans, due to the better performance of the U.S. economy. The cotton consumption estimates for MY 2002/03 and 2003/04 have remained unchanged at 2.1 million bales.

Mexico's National Textile Industry Chamber (CANAITEX) pointed out that two main factors are preventing a further expansion of cotton consumption in MY 2004/05. First of all, Mexico has been losing market share to China in the U.S. market in the last few years; and second, domestic consumption continues to be adversely impacted by illegal apparel/textile imports mainly from Asian countries.

Mexico's apparel and textile industry continues to be heavily dependent on exports, with 66 percent of production exported and 41 percent used domestically. According to the National

Apparel Industry Chamber (CNIV), however, these proportions have changed in the last few years due to the strong competition from China in the U.S. market. In CY 2000, for example, 71 percent of total textile and apparel production was exported, while the rest was consumed domestically.

TRADE

Due to the increased domestic production, cotton imports are forecast to increase just 1 percent in MY 2003/04 to 1.515 million bales. Again, the United States is expected to continue being the main supplier. At the same time, Mexican exports are forecast to remain unchanged in MY 2004. Asian countries will continue to be the largest export markets for Mexican cotton. The Mexican cotton import and export estimates have been revised upward in MY 2002/03 and 2003/04, reflecting official data from the Secretariat of Economy (SE) as well as updated industry information.

Under the North American Free Trade Agreement (NAFTA), Mexico's tariffs on cotton imports were phased out on January 1, 2003. Also under NAFTA, the rules of origin for cotton textiles products (such as fiber and yarn forwarding provisions) ensure that only textiles from NAFTA countries benefit from tariff reductions. The following cotton products are subject to NAFTA rules of origin: a) Fiber-forward: cotton yarns; cotton knit fabrics; b) Yarn-forward: most cotton woven fabrics; most cotton/man-made blends; c) Fabric-forward: cotton luggage, handbags, flat goods, cotton fabrics that are coated, laminated, or impregnated; d) Single substantial transformation: men's shirts from certain high-count cotton fabrics; men's shirts from certain cotton/man-made blends; apparel from specific fabrics (corduroy, velveteen).

In FY 2003, Mexican cotton importers used US$ 82.80 million of GSM-102 credit against US$ 69.4 million used in FY 2002. For FY 2004, GSM-102 is expected to continue to stimulate additional sales.

STOCKS

Due to higher production and imports than previously estimated in MY 2002/03 and MY 2003/04, stocks have increased from our previous forecast and estimate. Mexican mill owners have stated that an 8 to 10-week supply of cotton is sufficient to ensure adequate stocks. Due to continued tight credit and high interest rates, mill owners are reluctant to hold stocks for long. For MY 2004/05, with total consumption expected to increase to 1.515 million bales in MY 2004/05, ending stocks are expected to decline approximately 135,000 bales to 563,000 bales. The decrease in carryover is expected to reduce the stocks-to-use ratio from 32.8 to 25.9 percent.

MARKETING

The challenge for U.S. exporters in Mexico in the near future is to maintain their share of the Mexican textile market in the face of increasing domestic production, a decline in the Mexican textile industry, and potential challenges from third-country suppliers. The U.S. industry should continue to increase Mexican consumers' awareness of the advantages of cotton textile products. Cooperators should continue promoting the consumption of natural fiber products over synthetics. The United States has a distinct commercial advantage with its close proximity to Mexico, which permits cotton purchases on an "as needed basis." Moreover, the availability of credit terms offered under the GSM-102 commercial credit guarantee program improves the standing of U.S. cotton vis-à-vis other countries. U.S. cotton bales include fiber classification labels called HVI as well. According to CANAITEX these fiber-defining systems alleviate the millers's task by increasing handling and processing efficiency.

TEXTILE INDUSTRY

Total textile output fell 8.9 percent in CY 2003, the steepest decline since the severe contraction in CY 2001. CANAITEX blamed the slump in textile output –- now in its third consecutive year – on growing competition in the United States textile and apparel market from lower-cost Asian and Caribbean countries as well as on the strong peso against dollar since 2002 and part of 2003. Moreover, the domestic textile sector continues to experience high levels of smuggling and relatively high costs of production while simultaneously facing sluggish demand from the apparel sector, which also has been adversely impacted by the contraband. According to the CNIV approximately 60 percent of apparel purchased in the Mexican market is contraband. CNIV estimates total Mexico's apparel consumption at US$ 16.3 billion, of which US$ 9.4 billion are illegal imports, US$ 3.5 billion are official imports (with origin certificate), and US$ 3.4 are legally-produced products. The negative output trend is expected to continue during CY 2004, albeit at a slower pace than a year earlier, assuming that the U.S. economy continues its recovery.

Following are figures showing the average output growth rates for the Mexican textile industry:

Year	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
%	3.7	-5	-7	1.1	-6.3	15.7	10.5	3.9	3.1	5.4	-8.6	-5.8	-8.9

Source: National Institute of Geography, Statistics and Computer (INEGI).

As in production, CY 2003 textile exports decreased 8.3 percent compared to 2002, whereas textile sales for the "maquila" industry (in-bond industry), which are typically exported, decreased 10.4 percent for the same period. According to the National Institute of Statistics and Geography and Computer Science (INEGI), employment in the textile sector decreased 9.5 percent in 2003, compared to 2002. As a result, CANAITEX estimated a loss of approximately 132,000 jobs in 2003. Similarly, the number of workers in the apparel industry decreased 11.5 percent from 514,000 in CY 2002 to 455,000 in CY 2003.

The textile industry primarily produces yarns and knitted and woven fabrics, with denim fabric being a specialty. Traditionally, these fabrics have been sold to domestic apparel manufacturers. The majority of the textile firms are located in the central part of the country (Puebla, Tlaxcala, Mexico and Guanajuato). Industry sources pointed out that approximately 40 percent of the textile firms are family-owned, employing fewer than five employees. Leading Mexican textile firms exporting to the U.S. market includes Kaltex, S.A., Lear Mexican Trim, and Eagle Trading Co.

As already noted, CANAITEX and CNIV complain that the smuggling of illegal textile products continues to harm their industries, in spite of efforts by the federal government. The contraband is mainly of Asian and Chinese origin. As a result, both chambers have petitioned the Mexican Ministries of Treasury (SHCP) and Economy (SE) to intensify measures to control those practices.

Both industries recognize that they are becoming less competitive in several aspects. However, they are counteracting this by cutting costs as well as shifting production from low-value-added basic garments to more value-added garments and complete services. Industry sources are optimistic that if they are able to differentiate their products and move more into U.S. niche markets, production levels could be maintained and Mexico could continue to be a major supplier of textiles and apparel to the United States. Another factor, which could stimulate the Mexican textile sector, is the U.S.-Central American Free Trade Agreement (CAFTA). This agreement includes an accumulation clause, which would allow the Mexican textile industry to export fabrics to Central American countries to produce garments, then export these garments to the United States and still retain preferential access. CANAITEX pointed out it could increase Mexican textile exports.

At the same time there is growing concern in the apparel and textiles industries about the effects the 2005 elimination of the Multi-Fiber Agreement (MFA) will have. This agreement allows an importing signatory country to apply quantitative restrictions (quotas) on textile imports when it considers them necessary to prevent market disruption. The objective of the MFA was to reconcile the interests of textile-exporting and textile-importing countries by permitting an orderly expansion of trade while avoiding market disruption. But the global system of bilateral textile and apparel quotas that comprise the MFA is scheduled to end on July 1, 2005. The Mexican apparel and textile industries are concerned that the overall output of both industries could decline further once the MFA quotas are removed as China would continue to increase its market share in the U.S. apparel and textile markets. Consequently textile and apparel industries have been lobbying the Mexican government to enact measures, which would allow them to be more competitive. For example, the textile industry is requesting an exemption of the 2-percent tax on assets for those companies that invest in their plants during next two years; this tax has to be paid on assets (i.e., equipment) whether or not it is being used. Another request is for a reduction on electricity tariffs, which the textile industry claims are extremely high. Also, the Mexican textile industry will request that the SE continue compensatory quotas on Chinese garments and textile products. Despite the fact that China joined the WTO at the end of 2001, Mexico made a bilateral deal to keep high tariffs (approximately 500 percent) on certain Chinese products for another six years.